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**FISCAL IMPACT STATEMENT**

**LS 7288**

**BILL NUMBER:** HB 1118

**NOTE PREPARED:** Jan 11, 2005

**BILL AMENDED:**

**SUBJECT:** Health Insurance Premium Deduction.

**FIRST AUTHOR:** Rep. Espich

**FIRST SPONSOR:**

**BILL STATUS:** As Introduced

**FUNDS AFFECTED:** X GENERAL  
X DEDICATED  
FEDERAL

**IMPACT:** State & Local

**Summary of Legislation:** The bill provides a deduction in computing Adjusted Gross Income for amounts an individual spends during the taxable year on health insurance premiums for coverage of the individual, the individual's spouse, or a dependent. The bill also makes a technical correction.

**Effective Date:** January 1, 2005 (retroactive).

**Explanation of State Expenditures:** The Department of State Revenue (DOR) would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to incorporate this deduction. These expenses presumably could be absorbed given the DOR's existing budget and resources.

**Explanation of State Revenues:** (Revised) *Summary:* The bill would reduce state Adjusted Gross Income (AGI) Tax liabilities for individual taxpayers with premium expenses for certain health insurance coverage. The revenue loss due to this bill could potentially total as much as \$60.3 M beginning in FY 2006. Growth in the deduction could potentially range from 8% to 12% annually thereafter based on recent annual trends in medical expenses and health insurance premiums.

*Background:* The bill establishes a deduction from Indiana AGI for premiums paid by an individual taxpayer for health insurance coverage (as defined under the federal Internal Revenue Code) for the taxpayer, the taxpayer's spouse, and the taxpayer's dependents. The deduction is allowable regardless of whether the health insurance is obtained on an individual or group basis. Eligible premium expenses include: (1) premiums paid by an individual for private non-group health coverage; (2) employee premium expenses related to employer-

provided health coverage as long as the employee premiums are not paid with “pre-tax income; and (3) premiums paid by individuals for coverage through the Indiana Comprehensive Health Insurance Association (ICHIA). However, the bill provides that premiums paid by an individual for federal Medicare coverage, long-term care insurance policies, and Medicare supplement insurance policies are not deductible.

The table below reports the estimated revenue loss for the first year of the deduction by expense type. The fiscal impact of this deduction could potentially increase 8% to 12% annually based on recent annual trends in medical expenses and health insurance premiums. The growth rate would depend on a number of factors including year-to-year changes in health insurance coverage rates, employee participation in pre-tax payment plans, and the extent to which employers providing health insurance benefits share the cost of premium increases with covered employees.

Type of Expense	Revenue Loss from Expense Deduction
Private Non-Group Health Coverage	4.2 M
Employer-Provided Health Coverage	54.6 M
ICHIA Coverage	1.5 M
<b>Total</b>	<b>\$60.3 M</b>

*Estimation Background:* Deductible premium totals are estimated based on *Census 2000* population counts for Indiana and statistical results from various health insurance surveys. Information used for the different estimates is outlined below.

Private Non-Group Health Coverage: The deductible premium total for private non-group coverage is estimated based on survey research suggesting that roughly 5% of the population under the age of 65 is covered by such insurance policies, with current annual premiums averaging about \$1,530 for single coverage and \$2,890 for family coverage. In addition, this is adjusted to account for individuals who purchase private non-group coverage but already utilize the deduction from federal gross income for self-employed health insurance premiums. In 2001, 73,149 federal filers residing in Indiana claimed \$170.3 M in health premiums under this deduction. These premiums are excluded from the estimate.

Employer-Provided Coverage: Deductible premiums for employees with employer-provided coverage are estimated based on survey research suggesting that about 70% of the population under the age of 65 is covered by employer-provided health insurance, with the current employee share of premium cost averaging about \$560 for single coverage and \$2,660 for family coverage. This estimate is also based on survey research estimating that about 28% of workers are employed by businesses that offer “cafeteria plans” enabling workers to pay for employer-provided health insurance benefits with “pre-tax income. Thus, the estimated revenue loss attributable to premiums paid by workers for employer-provided coverage is adjusted to account for this group. To do so, it is assumed that government workers and 28% of private sector employees currently pay health insurance premiums with “pre-tax income.

ICHIA Coverage: Deductible ICHIA premiums are estimated based on annualized premium totals reported for the January-September 2004 period, and average ICHIA client totals for the same period. These totals are

adjusted to exclude clients whose premiums are paid by the Indiana Department of Health.

**Explanation of Local Expenditures:**

**Explanation of Local Revenues:** The proposed deduction could potentially decrease taxable income. As a result, counties imposing local option income taxes (CAGIT, COIT, and/or CEDIT) could potentially experience a significant decrease in revenue from these taxes.

**State Agencies Affected:** Department of State Revenue.

**Local Agencies Affected:** Counties with local option income taxes.

**Information Sources:** OFMA Income Tax databases, 1998-2001. *Census 2000, Age Distribution of Population, Indiana*, Summary File 1, <http://www.census.gov/>. Kaiser Family Foundation, *The Economic Downturn and Changes in Health Insurance Coverage 2000-2003*, September 2004, <http://www.kff.org/>. Kaiser Family Foundation, *Update on Individual Health Insurance*, August 2004. Kaiser Family Foundation, *Employer Health Benefits Annual Survey, 1999& 2004*. Bureau of Labor Statistics, *Employment, Hours & Earnings (NAICs Based Data) - Indiana: September 2004*. Ann Bingman, Affiliated Computer Systems.

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